Zacks Small-Cap Research

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Corporate Resource Services (CRRS-NASDAQ)

CRRS: *1Q14 Highlights; Believe Company On-Track to Regain Listing Compliance*

Current Recommendation	**Hold**
Prior Recommendation	Buy
Date of Last Change	6/04/2014
Current Price (08/28/14)	$1.75
Six- Month Target Price	**$2.90**

OUTLOOK

Corporate Resource Services (CRS), a rapidly growing temporary staffing company with an ambitious M&A strategy, reported results for its 1Q 2014. On an organic basis, CRS generated revenue growth of roughly 7.7% y/y compared to an estimated 2-2.5% increase for the industry, based on data from the American Staffing Association.
We also believe the filing of its 1Q 2014 results is a significant step towards achieving compliance with Nasdaq listing requirements.

SUMMARY DATA

52-Week High	**$5.62**
52-Week Low	**$1.81**
One-Year Return (%)	**-56**
Beta	**0.54**
Average Daily Volume (sh)	**152,553**
Shares Outstanding (mil)	**158**
Market Capitalization ($mil)	**$277**
Short Interest Ratio (days)	**8.1**
Institutional Ownership (%)	**0**
Insider Ownership (%)	**93**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**78.0**
Earnings Per Share (%)	**N/A**
Dividend (%)	**N/A**
P/E using 2013 Actual	**102.5**
P/E using 2014 Estimate	**17.5**
P/E using 2015 Estimate	**8.0**
Zacks Rank	**2**

Risk Level	**Above Average**
Type of Stock	**Small-Growth**
Industry	**Business Svcs**
Zacks Rank in Industry	**6 of 35**

ZACKS ESTIMATES

Revenue
(in millions of $)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)*
2012	145 A	154 A	180 A	201 A	680 A
2013	194 A	199 A	209 A	217 A	820 A
2014	218 A	243 E	255 E	269 E	986 E
2015					1,200 E

Earnings per Share
(EPS is operating earnings before non recurring items)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2012	-$0.02 A	-$0.01 A	$0.01 A	$0.01 A	-$0.01 A
2013	$0.00 A	$0.01 A	$0.03 A	-$0.02 A	$0.02 A
2014	-$0.02 A	$0.04 E	$0.04 E	$0.04 E	$0.10 E
2015					$0.22 E

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Zacks Projected EPS Growth Rate - Next 5 Years % **N/A**

*FY end has changed to Dec.in 2013 Disclosures pg 8

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KEY POINTS

- Corporate Resource Services (CRS) reported results for its 1Q 2014 on August 19, 2014. We believe this is another step towards the company's regaining compliance with the Nasdaq listing requirements.
- Despite that the 2013 quarter encompassed 14 weeks versus 13 for the comparable period of 2014, the company registered an impressive 12.5% revenue increase to $218.4 million and a roughly 7.7% increase, on an organic basis.
- Excluding non-cash and non-recurring charges, adjusted EBITDA came in at $3.9 million versus $2.5 million recorded in 1Q13.
- Nasdaq has given CRS until September 29, 2014 to catch up on all of its late filings in order to regain compliance. Management expects to meet the deadline. If it does not, CRRS shares could be delisted from the Nasdaq.
- On June 27, 2014, CRRS shares were added to several Russell Indices. Trading volume jumped from 162,400 to 1,766,700 on June 27, with the 30-day average remaining above the pre-inclusion level.
- We believe risks include that the shares are delisted from Nasdaq if CRS does not meet the deadline, that EPS could be lumpy over the next several quarters, competition could increase, the industry could be hurt by changing economic factors and that CRS is essentially a controlled company.

1Q 2014 HIGHLIGHTS

Corporate Resource Services (CRS) has reported results for its 1Q 2014, which we believe is another step towards the company's regaining compliance with the Nasdaq listing requirements. Despite that the 2013 quarter encompassed 14 weeks versus 13 for the comparable period of 2014, the company registered an impressive 12.5% revenue increase to $218.4 million, partly reflecting the impact of M&A transactions. Staffing companies that CRS acquired in late 2013 and during 1Q14 contributed revenue of $24.2 million. On an organic basis and excluding the impact of the extra week in the 2013 first quarter, the company generated revenue growth of roughly 7.7%. That rate compares to an estimated roughly 2-2.5% increase for the industry, based on data from the American Staffing Association. It is also impressive, we believe, in light of the severe weather during the period and the company's continued elimination of several unprofitable accounts, per a strategy launched in late 2013.

Gross Margins

CRS intends to expand its gross margins by **diversifying its service offerings towards higher margin services, improving its pricing structure and managing unemployment claims to reduce state unemployment taxes**. Management expects these initiatives to contribute to gross margin improvement over time. Nevertheless, 1Q14 margins were negatively impacted by CRS's growth in the lower margin light industrial businesses. The company's gross margin came in at 11.0%, down slightly compared to 11.1% registered in 1Q13. The company is working to shift its service mix to higher margin services including temporary professional staffing service and has registered strong growth in this category, albeit off a low base. Given the significant amount of business that CRS currently derives from lower margin light industrial sectors, it could take some time before the expanding professional services category impacts consolidated gross margins in a meaningful way, in our view. The company's continued roll-out of its higher margin software offerings is also expected to contribute to margin expansion.

In 2013, the company was also able to lower the fee that it pays to Tri-State, the affiliated company that provides certain PEO (Professional Employer Organization) administrative services to CRS, including payroll services, workers' compensation coverage and payroll tax and employee benefit plan administration. This fee fell to 1.4% from 2.0% and CRS believes there may be opportunities to lower it further. CRS accounted for 37.5% of Tri-State's aggregate administrative fee revenue in 2013. In the first quarter 2014, the administrative fee to Tri-State declined by roughly 400 basis points, reflecting the company's modified agreement.

Separately, CRS' acquisition of FlexPlus (see below) gave the company FlexPlus' *iintegra* software, which CRS intends to launch across its U.S. operations. *iintegra* is a job posting and applicant tracking system and management believes the roll-out will help with its targeted gross margin expansion.

Higher EBITDA

Reflecting higher costs, much of which was non-recurring and related to the change in auditors and efforts to regain compliance, operating expenses increased 20.9% year-over-year. This contributed to an operating loss of ($415,000) compared to positive $1.4 million registered in the same period of 2013. The loss also reflected non-cash stock compensation expense of $1.2 million compared to $324,000 million registered in the prior year period. Nevertheless, because many of these charges were non-cash or non-recurring, adjusted EBITDA came in at $3.9 million versus $2.5 million recorded in 1Q13. The company registered a net loss of ($3.0) million versus ($0.4) million recorded in 1Q13. We are updating our projections to reflect the company's first quarter 2014 results.

BELIEVE COMPANY ON-TRACK TO REGAIN COMPLIANCE

On June 23, 2014, CRS submitted a plan to the Nasdaq to regain listing compliance. The company filed its FY 2013 10K and FY 2014 1Q on July 1, 2014 and August 20, 2014, respectively. Once CRS submits its 10Q for its second quarter of FY 2014, we believe the company will have caught up on all of its delinquent filing requirements.

Nasdaq has given CRS until September 29, 2014 to catch up on all of its late filings in order to regain compliance. **Management expects to meet the deadline.** If the company does not file its financial statements by the September 29, 2014 deadline, CRRS shares could be delisted from the Nasdaq.

EXPANDING FOOTPRINT

The company continues to pursue smaller tuck-in acquisitions to expand its staffing footprint. CRS has purchased two staffing companies thus far in 2014: Staff Management Group and Alar Staffing. They added a combined roughly $115 million in annual revenue.

New Jersey based Staff Management Group is expected to contribute roughly $85+ million in annual revenue. The acquisition also strengthened the company's position in the New Jersey staffing sector. Management believes that with Staff Management Group, **CRS has become the leading staffing provider in the state of New Jersey.** In turn, we would expect this to lead to greater opportunities for higher margin contracts.

In November of 2013, CRS purchased U.K.-based Flex Recruitment Plus, its first offshore acquisition. The management team at FlexPlus has remained to oversee CRS' planned expansion within the European market, as the company has indicated that it is pursuing additional U.K. recruitment firms.

Earlier this month on August 5, 2014, the company promoted Flex Recruitment founder Adrian Hobbs to Executive Vice President of its European Operations to manage its growth plans in Europe.

RECENT NEWS

- On August 19, 2014 the company reported 1Q14 results and filed its 1Q14 10Q on August 20, 2014.
- On August 5, 2014, the company promoted Flex Recruitment founder Adrian Hobbs to Executive Vice President of its European Operations to manage its growth plans in Europe.
- The company filed its FY 2013 10-K on July 1, 2014.
- CRS submitted its compliance plan to Nasdaq to regain listing compliance on June 23, 2014.
- CRS amended its agreement with Wells Fargo on June 20, 2014, extending terms through June 30, 2015. The Wells Fargo agreement provides for up to $80.0 million in financing of receivables at LIBOR + 4.25% - 6.17%. Management hopes to replace this with a line of credit before the Wells Fargo agreement ends on June 20, 2015.
- On June 27, 2014, CRRS shares were added to the Russell Microcap, Russell 3000 and Russell Global indices. Trading volume in CRRS shares jumped from 162,400 to 1,766,700 on June 27.

RISKS

- We believe the company faces the risk that its shares are delisted from Nasdaq if it cannot file its 10Q on time.
- Quarterly results could be lumpy over the next several quarters.
- Competition could increase. The temporary staffing industry is one with few barriers to entry, we believe.
- Customers could shift towards hiring permanent employees instead of using temporary workers.
- Economic factors could constrain industry growth.
- The industry is populated heavily with mom & pops. As other, larger players acquire smaller operations, it could drive up costs of future acquisitions for CRS.
- The company's diversification efforts with Summit Software and Abest might take longer than expected or not be successful.
- We believe among the biggest risks is that CRS is essentially a controlled company, with significant related party transactions, and insider interests could conflict with those of outside shareholders.

INSIDER TRADING AND OWNERSHIP

In 2009, privately-held Tri-State Employment Services gained control of CRS. Robert Cassera, a member of the company's board, owns Tri-State Employment Services and beneficially owns roughly 90% of CRS shares. Other insiders, including the management team, hold another 2.5%, for total insider holdings of about 92.5%. This sizable insider ownership is a double edged sword, in our view. On the one hand, management's investment in the company creates strong interest in driving growth and share price appreciation, in our view. On the other hand, it also makes the shares highly illiquid and therefore difficult for outside investors to accumulate any meaningful stake.

We would expect insiders to reduce their holdings over time to enable outside investors to participate. CRS shares moved from the OTC market to the Nasdaq on September 6, 2013, which could also enhance the company's trading liquidity over time, in our view, as more shares enter the free float. We believe their inclusion in the Russell indices could also provide a sustainable improvement to trading liquidity.

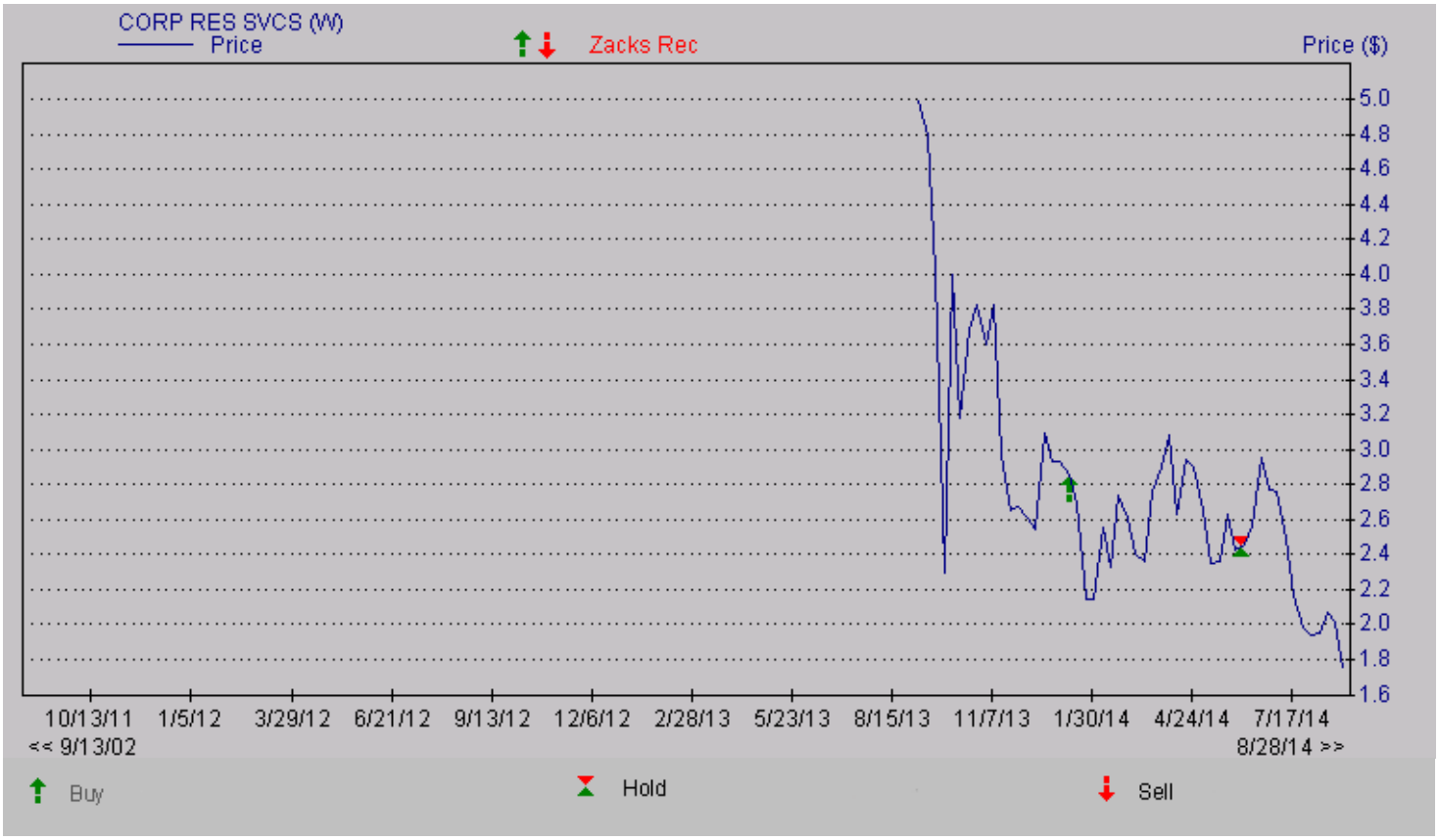
PROJECTED INCOME STATEMENT

Corporate Resource Services Income Statement & Projections ($000 except per share data)

	2012A	Pro Forma PF 1Q13	2Q13	3Q13	4Q13A	2013A	1Q14A	2Q14E	3Q14E	4Q14E	2014E
Revenues	679,839	194,217	199,195	208,957	217,304	819,673	218,410	243,018	254,928	269,457	985,812
Direct cost related	596,166	172,298	175,197	182,256	187,482	717,233	194,182	211,255	221,609	234,239	861,285
Direct cost	3,643	271	972	784	4,037	6,064	155	1,069	1,020	1,078	3,322
Gross profit	80,030	21,648	23,026	25,917	25,785	96,376	24,073	30,693	32,299	34,140	121,206
S,G&A - related	47,864	14,286	12,176	12,058	10,575	49,095	12,948	13,974	14,658	15,494	57,074
S,G&A	25,717	5,247	6,660	7,660	9,725	29,292	9,162	8,506	8,922	9,431	36,021
D&A	2,012	391	363	466	574	1,794	1,144	392	466	575	2,577
Other	1,264	324			5,264	5,588	1,234				
Operating income	3,173	1,400	3,827	5,733	(353)	10,607	(415)	7,822	8,252	8,641	24,300
Interest expense	4,344	1,166	1,407	927	946	4,446	980	984	988	992	3,944
Int expense related	861	359	422	464	448	1,693	691		-	-	691
Acquisition exp	144	-	32	34	-	-		-	-	-	-
Other exp (inc)	669	205	10	24	745	1,080	943	947	951	954	3,795
Net inc / (loss)	(1,219)	(330)	1,956	4,284	(2,522)	3,388	(3,029)	5,891	6,314	6,695	15,871
Noncontrolling interest		-	(71)	(113)	(428)	(612)	(18)	(18)	(18)	(18)	(72)
Taxes	518	48									
Net income (loss)	(1,737)	(378)	2,027	4,397	(2,950)	2,776	(3,047)	5,873	6,295	6,676	15,798
EPS											
Diluted	($0.01)	($0.00)	$0.01	$0.03	($0.02)	$0.02	($0.02)	$0.04	$0.04	$0.04	$0.10
Avg shares out (FD)	148,377	159,433	158,422	162,896	169,317	162,517	158,015	159,015	160,015	161,015	159,515

Source: Company reports, Zacks Small Cap Research Estimates

HISTORICAL ZACKS RECOMMENDATIONS



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